Supreme Court of the United States

ELLA FRAD,
Plaintiff-Petitioner,

against

THE COLUMBIAN NATIONAL LIFE INSURANCE COMPANY,
Defendant-Respondent,

against

ELLA FRAD, as Executrix under the Last Will and Testament of William D. Frad, deceased,
Third Party Defendant.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Respondent respectfully submits that the case at bar is unique in its facts; the ruling of the Court of Appeals is narrow in its application; there is nothing to warrant special attention by this Court; and finally, the point has been reached, at long last, when this litigation should be permitted to come to an end.

The Facts.

The evidence produced at the trial showed that in 1928 and 1929, defendant issued to William D. Frad, three policies of life insurance which provided, all together, for the payment of $20,000 to Ella Frad, his wife, upon his death; and for the waiver of premiums and payment of $200 a month in the event of his total and permanent

disability (Pltf's Exs. 5, 6 and 7; admitted p. 163, printed p. 262-5). In his application for each of these policies, Frad represented that he was a clothing salesman.

In November 1935, Frad made claim for disability benefits, asserting that he was totally and permanently disabled by a heart condition (ff. 820-825). Investigation of this claim then revealed that Frad was not a clothing salesman but an international cardsharp who had spent the past two years in the Federal Penitentiary for having obtained and used false United States passports in the name of "Frederick Warren Gorham," and a false Canadian passport in the name of "Daniel Edward Swift" (ff. 1159-1160; 1439-1440).

Although defendant would, no doubt, have refused to issue the policies had it known that Frad was a cardsharp, the policies had become incontestable and therefore on the advice of its examining physician that the insured had a serious heart condition (f. 852), defendant approved the claim (f. 830), waived premiums, and paid disability benefits from January 1936 through July 1937 (Deft's Ex. II; admitted p. 207, printed p. 397).

When defendant then learned that Frad had taken more than $30,000 from a man named Richter on the SS *Santa Rosa* in October 1936, and had probably participated in still another card game (ff. 1058, 1347-1350), it refused to pay further disability benefits (ff. 97-100). Thereupon Frad brought suit in the City Court of the City of New York to compel defendant to continue the disability payments, but, before the action could be brought on for trial, he was returned to the Federal Penitentiary where he remained until the spring of 1939 (ff. 1056-1058; 1439-1440; 1451, 659 and 662). Upon his release, his action was brought on for trial in the City Court and settled by the payment of $4,696.55 in compromise of accrued benefits of some $6,000 (ff. 809-812); and defendant thereupon re-

opened the claim, waived premiums, and paid disability benefits until April 1940 (f. 1191).

Upon receipt of information that Frad had again engaged in card games for money, defendant, for the second time, terminated its payments (ff. 115-117, 1351-1353), and Frad once more brought suit to compel defendant to continue the payments. This time the Municipal Court of the City of New York was the forum and defendant not only denied its liability to pay further benefits but asserted a counterclaim for the recovery of the benefits which it had already paid (ff. 756-764).

An intensive and singularly successful investigation was then undertaken by defendant which yielded an impressive amount of evidence concerning the activities in which Frad had been engaged while collecting disability benefits and enjoying a waiver of premium (ff. 632-637). This evidence, which has been collated in defendant's exhibits GG-1 and GG-2 (admitted p. 205, printed pp. 393-4), indicated that from 1929 to 1942, Frad's constant occupation when not under Federal detention had been to cheat at cards for high stakes. Although the pattern of his operations was always the same, he underwent several changes of identity in the process, and with each change associated himself with a new set of companions.

From May 1929 to June 1931, travelling under a false United States passport, he worked the North Atlantic as "Frederick Warren Gorham" of the Gorham Silver Company. His companions were Messrs. Davis, Mull and Schwartz (Deft's Exs. GG-1). Colonel John C. Minor, who lost $19,090.80 at "old fashioned bridge" on board the SS *Paris* in June 1929, was one of the victims of this period (ff. 509-534), which was brought to an end by Frad's first indictment for passport frauds on June 16, 1931 (f. 1438).

From June 1932, to November 1933, travelling under a false Canadian passport, Frad continued to work the North Atlantic, but now he was "Daniel Edward Swift", a Cana-

dian meat packer (f. 1160), and his companions were Messrs. Ashcroft, Buttolph and Bowen (Deft's Ex. GG-1). This period was brought to an end in February 1934, by his second indictment (f. 1439), arrest and conviction (ff. 659-660).

For a few months in 1936 after his release from the Federal Penitentiary, Frad sailed under his own name with several of his old companions on vessels cruising to the Caribbean and to California (Deft's Ex. GG-2). This gave him an opportunity to take nearly $32,000 from Francis G. Landon on the SS *Rotterdam* in August 1936 (ff. 1201-1203), and to "win" $36,000 (later compromised at $18,000) from Paul K. Richter on the SS *Santa Rosa* in October 1936 (ff. 686-687, 1056-1058). This brief interlude under his own name was terminated when the insured was arraigned and remanded for violation of his parole in November 1936 (f. 660), but this did not put an end to his depredations for he sued out a writ of habeas corpus which was sustained and then, while the case was taken first to the United States Court of Appeals for the Second Circuit (*Kelly, Marshall* v. *United States ex rel Frad,* 89 F. 2d, 865), and then to this Court (*Frad* v. *Kelly,* 302 U. S. 312), he resumed his activities as "Daniel Fulton", millionaire operator from Oklahoma. "Fulton" was even more successful than "Gorham" and "Swift" had been in taking substantial sums of money from elderly gentlemen at crooked cards. With the assistance of Messrs. Hudson and Daly (Deft's Ex. GG-2), "Fulton" took $13,300 from William T. Dowling on board the SS *Columbus* in April 1937 (ff. 1204-1217); $96,000 from George A. Ball on board the SS *Reliance* in June 1937 (Deft's Ex. GG-2; ff. 682, 1440); $47,000 from Alexander Glass in September 1947 (Deft's Ex. GG-2; ff. 683-684); and $6,217 from Professor Charles Cheney Hyde on board the SS *Columbus* in October 1937 (Deft's Ex. GG-2; f. 1218). This very lucrative period came to an end in November 1937 when this Court sus-

tained the order of the Court of Appeals and "Fulton" returned to the Federal penitentiary to serve the balance of Frad's sentence (*Frad* v. *Kelly, supra*).

Released again in the spring of 1939 (f. 661), Frad immediately picked up where he had left off and, once more using the name of "Daniel Fulton", renewed his Caribbean cruises (Deft's Ex. GG-2). It was on one of these cruises, on the SS *Nieuw Amsterdam* in February 1940, that he took notes for $3,200 from C. Stowe Spencer (ff. 1263-1286), and for $3,125 from George A. Wedge (ff. 1240-1262). A few months earlier, in November 1939, assisted by Messrs. Raphael, Daly and Darnell, he had taken $15,925 from Frederick R. Sears at the Ambassador Hotel in New York (ff. 1287-1310); and in the following autumn, again with Darnell's assistance, he took some $15,000 from Eugene S. Halle at the Hotel Claridge in Atlantic City (ff. 1311-1343). How Frad fared thereafter the record does not reveal, except that he experienced at least one final change of name when he became "Thomas F. Hunt" who frequented fashionable hotels along the Atlantic seaboard (Deft's Ex. GG-2).

When all of this information had come into its possession in the late summer and early fall of 1942 (ff. 632 and 638), defendant amended its answer in the Municipal Court action so as to plead, as an equitable defense, that the policies had lapsed for non-payment of the premiums which had been erroneously waived in reliance upon the insured's representation that he was totally disabled (ff. 1418-1422), but at the trial of the Municipal Court action, this defense was struck out upon the ground that the Court lacked jurisdiction to entertain an equitable defense (ff. 625-626). Accordingly, the questions put to the jury were (1) whether the insured was disabled in April, May and June 1940, so as to be entitled to $600 in disability benefits, and (2) whether he had collected benefits for earlier periods when he was not entitled to them so as to be

liable on defendant's counterclaim for their recovery. The jury answered each of these questions in the negative but, on appeal, the judgment was vacated, in so far as it dismissed defendant's counterclaim, and the counterclaim was remanded for retrial (*Frad* v. *Columbian*, New York Law Journal, Vol. 109, 4/22/43, page 1562; *Frad* v. *Columbian*, New York Law Journal, Vol. 109, 6/17/43, page 2368). Instead of being re-tried, however, the counterclaim was discontinued (*Frad* v. *Columbian*, New York Law Journal, Vol. 111, 2/18/44, page 658), and reasserted in the action at bar.

This concludes the story of the issuance of the policies to the supposed clothing salesman in 1928 and 1929; the payment of disability benefits and the waiver of premiums for long periods of time when, unknown to the Company, he was engaged under various aliases and with various confederates in making thousands upon thousands of dollars at his usual and chosen occupation; the settlement of the City Court action for want of evidence to defend it; and, finally, the defeat of the Municipal Court action by the overwhelming evidence which was eventually marshalled against him.

A general knowledge of these events is essential to an understanding of the facts leading up to the surrender of the policies and the institution of the present litigation.

In January 1941, Frad applied to the Colonial Trust Company for a loan to be secured by the policies. The Municipal Court action was pending at that time but no claim had then been made that the policies had lapsed for non-payment of premiums erroneously waived, for the defendant had not then uncovered the evidence of Frad's activities which has been described above. Accordingly, when the Trust Company made inquiry of defendant concerning the status of the policies, it was informed that each policy was in force with no premiums in arrears and no loans outstanding, and that the loan and cash surrender

values exceeded the loan sought by the insured (ff. 118-131). Upon receipt of this information, the Trust Company loaned Frad $4,000 (subsequently increased to $6,300) on the security of the policies (ff. 174-176). The form of collateral assignment which was used for this purpose gave the Trust Company the *sole* right to surrender the policies and receive the cash values at any time. It also gave the Trust Company the *sole* right to obtain loans on the policies. Further, it authorized the insurer to recognize the assignee's claim to rights under the assignment without investigating the reason for any action taken by the assignee. In this same connection, it provided that the *sole* signature of the assignee would suffice for the exercise of any rights under the policies, that the *sole* receipt of the assignee of any sums received should be a full discharge and release to the insurer, and that checks for any sums payable under the policies should be drawn to the *exclusive* order of the assignee (ff. 1061-1076).

In September 1942, which was about a year and eight months after the loan was made, defendant, having uncovered Frad's very lucrative activities, amended its answer to the complaint in the Municipal Court action so as to allege that the policies had lapsed for non-payment of the premiums of which it had been defrauded. This, quite naturally, alarmed the Trust Company, which took the position that, as to it, defendant was estopped to claim that the policies had lapsed for non-payment of premiums (ff. 175-176).

On January 17, 1943, the loan went into default which, of course, made it necessary for the Trust Company to take some affirmative action. Having endeavored, in vain, to persuade defendant to recognize the estoppel which it claimed, or to make some other arrangement satisfactory to it (ff. 174-180; 1105-1121), the Trust Company, finally, made an absolute and unequivocal demand upon defendant for the cash surrender values of the policies (ff. 1147-1153).

Defendant complied with the demand (ff. 1156-1158). Soon afterwards Frad commenced the present action to have the transaction construed as if, instead of having been a payment of cash surrender values to the Trust Company, it had been a loan made to him on the security of the policies. He did not join the Trust Company as a party to the litigation.

One other phase of the matter should be mentioned before we turn to points of law raised by the pending petition. The beneficiary of the life insurance policies was the wife of the insured. After his death, she became the plaintiff in the action in her own right as beneficiary, and she is now the one who petitions for a writ of certiorari. She knew that her husband travelled under false passports; she knew that his occupation was to play cards for money; she was acquainted with the men who accompanied him on his card playing trips; she was familiar with the arrangement between her husband and his companions for the division of their "winnings"; she kept large amounts of cash for him in a safe deposit box; she knew he used assumed names in pursuing his occupation, and she, herself, used an assumed name in maintaining a safe deposit box to which he had access; she knew the names of quite a number of the men who were his victims (ff. 642-701, 703). When her husband was away on trips, it was she who endorsed his disability checks and deposited them in a joint account which she maintained with him (ff. 675-676, 1189-1191). In short, she was perfectly aware that he was gainfully employed at his usual occupation while collecting disability benefits from defendant and enjoying a waiver of premiums. She even assisted him in collecting the disability benefits, and she personally profited by the fraud.

Opinions Below.

On the foregoing evidence, the District Court held that defendant was entitled to recover from the estate of the insured (which was bankrupt) the disability benefits of

which it had been defrauded and the premiums which it had been fraudulently induced to waive. At the same time, the Court held that the beneficiary, who now petitions for certiorari, was entitled to recover the face amount of the insured's policies, less the cash surrender values which had been paid to the Trust Company and the premiums which had neither been paid nor waived. The heart of the decision, we believe, was the holding that once premiums have been waived, the only recourse open to the insurer, when it finds that it has been defrauded, is to bring an action against the insured as for a debt; and that it cannot declare the policies lapsed for non-payment of premium. This, we respectfully submit, is neither good law nor good sense.

On appeal, the Court of Appeals for the Second Circuit unanimously reversed the District Court and dismissed the complaint upon the ground (1) that the insurer could not have been compelled to make a loan to the Trust Company or to any one else, for the loan values of the policies had been exhausted by the insured's fraud; and (2) that neither the insured nor the beneficiary, who had kept the policies in force by fraudulently inducing the insurer to waive the premiums, came to the Court with clean hands and, hence, neither of them was entitled to have the policies reinstated.

POINT I.

There is no novel or substantial question which requires this Court's review.

Fortunately for the life insurance industry there can only be one William D. Frad, and he is dead. Fortunately, also, the litigation which he occasioned is essentially unique. Petitioner's contention that the decision of the Court of Appeals has swept away the rights of all insured persons, their assignees and beneficiaries, is patently absurd. What

petitioner's counsel is really trying to do is to induce this Court to assume the function of the Court of Appeals of the State of New York because her judgment has been reversed, but he is unable to assign any unusual or compelling circumstances to justify such a course. His plea that the Court below failed to follow the statutory and common law of the State of New York is no different from the plea which is always presented to an appellate court and has in it no factor which calls for special consideration by the United States Supreme Court.

POINT II.

The decision of the Court of Appeals does not conflict with the statutory law of the State of New York.

Over and over again in the petition and brief our opponent contends that the decision of the Court of Appeals violated Section 155(g) of the Insurance Law of the State of New York which requires insurers to lend money within the limits of the cash values of their policies.

Over and over again our opponent also contends that the decision violates Section 166(1)(5) of the Insurance Law which protects the "proceeds and avails" of life insurance policies for the benefit of third party beneficiaries as against the claims of creditors of the insured.

The answer to these contentions, as Judge CHASE so clearly puts it, is that each of the policies which are the subject of the present litigation expressly provides that *any* indebtedness to the Company on the policy will diminish the cash and loan values. In other words, in the language of Section 166(1), the "proceeds and avails" are to be determined only after the insured's indebtedness to the Company has been deducted. In the case at bar, the "proceeds and avails" must be identified as of the time when, if ever, defendant should have made a loan to the Trust

Company. This, of course, limits them to the cash and loan values, for the insured was then alive and the policies had not then matured as death claims.

Unlike the insured, the beneficiary never had any interest in the cash and loan values and, consequently, Section 166(1)(5) of the Insurance Law was not called into play. It could not protect her interest because she had none at that time. It did not even purport to protect his interest.

The insured, of course, would have had an interest in the cash and loan values, had they not been previously exhausted by his indebtedness to the Company. Because of this indebtedness, however, there was no obligation to make a loan to him or to make a loan for his benefit and, consequently, Section 155(g) of the Insurance Law was not violated. As Judge CHASE puts it:

> "The insurer, being obliged to make loans on the policies only to the extent of their existing loan values, was therefore free to refuse to make any loan on the policies for the benefit of the insured whose equities in the policies had been extinguished by his receipt of the proceeds of his own fraud" (p. 542).

Accordingly, we perceive no violation of the statutory law of the State of New York upon which the petitioner so heavily relies.

POINT III.

The decision of the Court of Appeals does not conflict with the case law of the State of New York.

Over and over again in the petition and brief our opponent contends that the decision of the Court of Appeals is contrary to the decisions of the courts of the State of New York, and, more particularly, runs counter to *Wilkes* v. *Equitable Life Assurance Society*, 262 App. Div. 73, modified 289 N. Y. 63; *Standard* v. *Equitable Life*, N. Y. Law

Journal 3/7/36 p. 1197, aff'd 247 App. Div. 617, aff'd 274 N. Y. 519; *Orent* v. *Equitable Life*, 268 App. Div. 299; and *Grauer* v. *Equitable Life*, 167 Misc. 30.

Our denial of this contention is twofold: first, the *Wilkes, Standard, Orent* and *Grauer* cases do not support the proposition for which our opponent cites them; and, second, the decision of the Court of Appeals does not conflict with them but, on the contrary, cites them correctly.

At page 12 of the petition, our opponent cites the foregoing cases for the proposition that "where an assured obtains disability benefits from an insurer by fraud * * * the insurer has a claim for debt as a creditor against the assured, but * * * this claim, just as any claim of any other creditor, is barred from being offset against the policies, or beneficial rights or interests therein of the assured or the beneficiary." In our opinion, these cases stand for no such proposition. They do not limit the insurer to a claim for debt as a creditor. Neither do they relate to the offset of claims against policies. The proposition for which they stand, and for which Judge CHASE correctly cited them on page 541 of his opinion, is that life insurance policies cannot be lapsed by the unilateral act of the insurer but only after the insurer has given the insured a new, reasonable time, fixed by the Court, within which to pay the arrears of premium.

Moreover, the cases in question should also be distinguished on their facts from the case at bar. In the case at bar, instead of meeting his obligation, fixed by contract, to pay premiums at stated intervals, the insured deliberately elected to defraud the Company by falsely contending that he was disabled. In the cited cases, with the exception of the *Orent* case, there was no fraudulent representation that the insured was disabled but only a claim that he had made some material misrepresentation, when, many years earlier, he applied for his insurance, and that, by reason of such misrepresentation, the insurer was entitled to rescind the disability coverage and retroactively

annul the waiver of premiums. In such circumstances, the New York courts have held that the insurer must prove the material misrepresentation before the insured can be called upon to pay the arrears of premium. To put the distinction another way, in the case at bar, the insured avoided his obligation to pay premiums by fraudulently representing that he was totally disabled, whereas in the cited cases, it was claimed that he had made a material misrepresentation when, originally, he applied for the insurance.

The *Orent* case, however, was like the case at bar in that the insured obtained a waiver of premiums by fraudulently representing that he was totally disabled. That case may nevertheless be distinguished because, when the insurer granted the waiver of premiums to *Orent*, it had ample notice of his fraud but, for reasons sufficient to itself, elected to continue to pay the disability benefits.

Accordingly, we perceive no conflict between the decision of the Court of Appeals in the case at bar and the decisions of the New York courts in the cases so frequently cited and so heavily relied upon by the petitioner.

POINT IV.

The decision of the Court of Appeals does not conflict with *Missouri State Life Ins. Co.* v. *Langreder.*

Over and over again in the petition and brief our opponent contends that the decision of the Court of Appeals conflicts with the decision of the Seventh Circuit in *Missouri State Life Ins. Co.* v. *Langreder*, 87 F. (2d) 810.

The short answer to this contention is simply to refer the Court to Judge CHASE's opinion at the top of page 542 in which he indicates, quite clearly, that it is not the intention of the Court to take issue with that case. Furthermore, it must be obvious that, since the *Langreder* decision was devoted to the interpretation of Illinois law, any conflict be-

tween that decision and the decision of the Second Circuit interpreting New York law would not be the type of conflict which should interest or concern this Court.

POINT V.

The Court of Appeals correctly held that the petitioner was not entitled to equitable relief.

As a second and quite independent reason for the dismissal of the complaint the Court of Appeals held that, since the insured and the beneficiary had defrauded the insurer and had retained the fruits of the fraud, the beneficiary (the insured having died) was no proper person to seek affirmative equitable relief.

It could not be gainsaid that the policies had, in fact, been surrendered or that without the intervention of a court of equity, they could never mature as death claims. As Judge CHASE pointed out in the concluding paragraph of his opinion, it is a fundamental rule that one who comes into equity must do so with clean hands. In this case nothing could be more clear then that both the insured and the beneficiary came to the court with unclean hands. Therefore, even if there were any merit to the petitioner's contentions, which we have just reviewed, the clean hands doctrine would, alone, suffice to sustain the decision of the Court of Appeals.

We make no special comment on Point VI of the petitioner's brief except to call the attention of the Court to the fact that in each one of the cases there cited the insurer was guilty of gross fraud in effecting the surrender of a policy of life insurance, whereas, in the case at bar, there is no proof and no finding that the insurer practiced any fraud of any kind but only that it asserted legal rights in the policies in contravention of rights claimed by the insured and the assignee.

CONCLUSION.

The petition for certiorari should be denied.

Dated: December 14, 1951.

Respectfully submitted,

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